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Cost Reporting	:	

INITIAL COMMENTS OF THE GREETING CARD ASSOCIATION

The Greeting Card Association (GCA) files these comments pursuant to Order No. 2163 (August 20, 2014).

The Commission attached to that Order the Postal Service's memorandum[1] and asked commenters to discuss it. The Service offered an extensive list of candidate activities, some of which could present conceptual difficulties, although we believe they can generally be evaluated using the Commission's current methods. The Commission has employed a "profitability" approach, developed in the 2008 USO Report[2] and regularly used in annually reporting the cost of sec. 3651(b)(1)(C) services and activities. As the Commission noted in Order No 2163 (p. 2), the only services thus far examined under paragraph (C) are six-day delivery and the unzoned structure of First-Class and Media/Library Mail. These services are revenue-producing mail categories purchased by the public, and analyzed in the Service's cost data systems.

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[1] Analysis of Additional Postal Service Activities That Could Qualify for Reporting Under 39 U.S.C. § 3651(b)(1)(C) ("Analysis").

[2] *Report on Universal Postal Service and the Postal Monopoly* (2008), ch. 4, especially pp. 112 et seq.

Some of the Postal Service's newly suggested candidates, however, do not fall under this description. In what follows, we consider some of these, from the standpoints both of eligibility for paragraph (C) reporting and of how they might be costed out, using the established profitability method.

Non-revenue-producing activities – law enforcement and in-house oversight. The Postal Service's Analysis lists a number of explicitly or implicitly mandated activities which might be eligible for paragraph (C) reporting. Two particularly important ones are the Postal Inspection Service (Analysis, pp. 10-11) and the Office of the Inspector General (id., p. 11). The former is required by 39 U.S.C. sec. 204, and the latter by sec. 410(b)(10) which carves out an exception for the Inspector General Act to the general inapplicability to the Service of Federal management statutes.

Both might be thought of as law enforcement entities, though the OIG also performs research studies. The Postal Service suggests that the Inspection Service's activities might be paid for from the general Treasury or assigned to an existing Federal law enforcement agency similarly funded. The Inspector General of any other agency would be supported by general Treasury funds, whereas the Postal Service's OIG draws on the Postal Service Fund.[3]

These are significant cost centers totaling $652.2 million – between five and six times the cost the Commission reports for unzoned First-Class and Media/Library rates.

Because these statutorily-mandated activities – unlike six-day delivery and unzoned rates – are not constitutive parts of specifically postal services purchased by the mailing public, it is worthwhile to consider how the profitability approach can be adapted to evaluating their cost.

[3] The Postal Service also notes that while a private-sector firm might perform similar internal audit functions, it would probably not set up an entirely separate entity for the purpose and incur duplicative costs as a result.

The Commission defined the profitability approach in its *Report on Universal Postal Service and the Postal Monopoly* ("USO Report"). At pp. 101-102, the USO Report states that

> . . . The second [i.e., profitability] approach compares profit levels under the status quo to profit levels under a "what if" scenario in which one element of either the USO or the monopoly is changed. The focus shifts to imagining how a profit-maximizing postal operator would respond to all aspects of the new commercial environment. . . . [T]he Commission evaluates changes to the Postal Service's current Universal Service Obligation and its current monopoly protections in terms of their impact on Postal Service profits.

This description suggests that the correct focus is on the *overall* profitability of the Postal Service when a change in the USO is hypothesized. The question raised by the potential expansion of the scope of paragraph (C) reporting, however, is whether this approach fits equally well when the activities being costed are not revenue-producing services.

At first glance – and from a simple bookkeeping perspective – there would appear to be little difficulty. If, e.g., Congress assigned all the functions of the Postal Inspection Service to the Federal Bureau of Investigation, and increased the FBI's appropriations correspondingly, the Service's net position would improve, ceteris paribus, by $410.7 million (Analysis, p. 11). The profitability approach is designed to measure the effects of changes on the postal operator, and not on the total budget of the Government.

We believe, however, that it is not quite that simple. It remains true that the profitability method was developed specifically to evaluate changes in the postal services offered to the mailing public (and, relatedly, in the limitations on similar services which the private sector might otherwise offer). The USO Report

(p. 113) itself suggests a reason for reviewing how the profitability approach should be used to estimate the cost of non-revenue activities:

> . . . Since it is pivotal to the preferred approach, great care is taken to identify the precise status quo being analyzed. The historical and legal analysis in this report focuses on what are, and are not, appropriately regarded as the Postal Service's current USO requirements and monopoly protections Without clearly defining these features of the current postal landscape, it is not possible to evaluate the impact of removing them.

The Commission was here explaining the clearly correct notion that if a given element is *not* in fact part of the USO, then eliminating it would be simply irrelevant to determining what the USO actually costs.

In the present context, we are concerned with whether a given service or activity would be continued, in whole or in part, if the law requiring it were repealed. Thus one defining feature is whether the Postal Service would find it useful or necessary *even absent a legal requirement* to provide the service or perform the activity in question. Continuing with our previous example: are there some Inspection Service functions which could not be performed, or performed equally effectively, by a different Federal law enforcement agency? Simple repeal of sec. 204, in other words, would not prohibit the Service from maintaining some internal law enforcement capability, but merely remove the requirement that it do so. For instance, it might be found that the Inspection Service's forensic laboratory functions could be reassigned without significant loss of value to the FBI, while the activities of the uniformed Postal Police Officers could not.[4] The answers to questions like these would clearly affect the cost side of the evaluation.

In short, just as the USO Report emphasizes that the existing USO must be accurately defined before the cost effect of changing (what appeared to be)

[4] These different functions of the Inspection Service are described in summary form at https://postalinspectors.uspis.gov/aboutus/mission.aspx.

one part of it can be ascertained, it seems necessary, in the case of legally required non-revenue activities, to decide what aspects of the activity the Service would continue to perform voluntarily if the legal compulsion were abolished. If those aspects were ignored, the Commission would risk overestimating the cost of functions which the Postal Service performs *only* because legally compelled to do so. We acknowledge that this might be a difficult, or at least a highly judgmental, process. For example, the Postal Service's reputation for reliability and for safe handling and delivery of mail is doubtless a substantial marketing asset. Would it be reduced in value if the Service's law enforcement activities were reassigned to another agency? If so, by how much? And what effect would such a reduction have on the revenue side of the equation?[5]

We emphasize that this discussion is not meant to suggest that the profitability method cannot be used to evaluate the cost of required non-revenue activities. It does seem, however, that the cost figures for such activities provided in the Service's Analysis can be only a starting point for any evaluation of their effect on profitability, considered from the standpoints of both avoided cost and revenue impact.

Program elements not directly affecting the mails. The Postal Service Analysis describes some programs in which it is legally required to participate, which impose costs that could be avoided if the programs were differently structured or if the Service were allowed to substitute programs of its own design. These programs share a significant property: they do not directly affect the provi-

[5] The Service's Analysis does not distinguish between two cases: funding of a specifically postal law enforcement agency from the general Treasury, and reassignment of the Inspection Service's functions to an existing agency (perhaps, e.g., the FBI). It would seem, however, that the profitability effects could be different. Tax-supported funding of a dedicated postal enforcement agency should, theoretically at least, lead to no change in the level and quality of postal law enforcement performance. Reassignment of those functions to another agency, in whose hands they would have to be fitted into a broader (and perhaps changing) system of enforcement priorities would offer no such assurance.

sion of postal services to the mailing public. Two particularly interesting examples are –

1. Required participation in the Federal Employees Health Benefit Program, which, as the Service points out (Analysis, pp. 4-6), does not integrate retirees' benefits with Medicare (including Part D drug benefits). Non-integration with Medicare, by raising the cost of retirees' health care, *eo ipso* inflates the Service's abnormally heavy prefunding obligation. According to the Postal Service (Analysis, p. 6), this factor, accounting for $43.8 billion in unfunded retiree costs, dwarfs the paragraph (C) activity costs so far identified by the Commission.

2. Required participation in the Federal workers' compensation program. See Analysis, pp. 12-14. The Service compares its situation with that of a private employer subject to state compensation rules, and points out that the Federal system allows a retirement-age claimant to continue receiving workers' compensation rather than switching to the (less generous) retirement benefit.

These examples are particularly interesting because they represent legal requirements to act in ways which arguably impose substantial additional cost without visibly improving or expanding postal services. As the Service notes (Analysis, p 3), sec. 3651(b)(1)(C) calls for reporting of mandates which "the Postal Service might not otherwise perform . . . or might perform . . . in a different way." The Service could be allowed to provide a health benefits program free of the inefficiencies it perceives in the present FEHBP. The same general observation applies to workers' compensation. Both seem to present clear examples of requirements, removal of which would allow the Service to reach the same ends in less costly ways. If, as the Commission's profitability approach assumes, the Service should be viewed as a profit maximizer, it seems to follow that the costs these inefficiencies are said to cause result entirely from a legal constraint.[6]

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[6] At p. 7 of its Analysis, the Postal Service discusses an alternative scenario in which it is still required to participate in FEHBP, but that program itself is reformed by requiring Medicare integra-

Comparisons with the private sector. As noted previously, the two elements which the Commission has reported under paragraph (C) – six-day delivery and unzoned rates – are properties of postal products offered to the mailing public. These are, by definition, elements in which comparisons of the Postal Service's obligation with supposedly analogous obligations faced by private-sector entities are out of place: the latter simply do not exist. The Service's Analysis, however, presents several items in which the suggested profitability effects are explained by comparing Postal Service (and, in most cases, government-wide) obligations with those affecting private-sector firms.

This fact suggests a question not raised by the two service and rate characteristics just mentioned: does "requirement of law," as used in sec. 3651(b)(1)(C), refer to an obligation imposed uniquely on the Postal Service, or does it include obligations which the Service faces simply because it is an "independent establishment of the Government of the United States" (39 U.S.C. sec. 101(a))?

The most obvious, and in GCA's view the correct, view is that "requirements of law" means what the dictionary suggests it means: there is *some* law which imposes a requirement on the Service, and the Commission is to ascertain whether the Postal Service would continue the required service or activity absent that law; if the latter question is answered "no," then the Commission is to report the cost of the service or activity. If Congress had instead said "requirements of this title," it might be argued that, e.g., the health benefit inefficiencies the Service must pay for by virtue of provisions in Title 5 fell outside the definition – though even this argument would be dubious, since it is Title 39 which requires the Service to participate in government-wide (Title 5) programs. GCA suggests, there-

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tion and providing a separate risk pool for postal employees and retirees. It may be worth considering whether this scenario represents a case of an activity in which the Service would not engage but for a legal requirement, or simply one in which positive profitability effects are secured not by relieving the Service of a legal obligation but by reforming the obligation itself.

fore, that reading sec. 3652(b)(1)(C) to encompass any requirement of law is appropriate.

Negative "requirements." At p. 2 of its Analysis the Postal Service raises and answers the question whether legal requirements to refrain from certain services or activities – assuming that they impose costs – are also eligible for reporting under paragraph (C). The Service concludes, correctly, that they are not. It goes on, however, to argue that

> . . . legal restrictions and prohibitions also impose implicit costs in terms of revenue opportunities foregone. Examples of these include the cap on market-dominant prices, the prohibition on new nonpostal services, prohibitions on carrying nonmailable matter (e.g., alcoholic beverages), and the prohibition on certain activities regarding address list information. Even if the Commission determines that these prohibited activities do not fall within the literal scope of Section 3651(b)(1)(C), they form part of the same legal context, and they may bear mention in the Commission's annual report to Congress.[[7]]

GCA believes that "mentioning" these items in the course of paragraph (C) reporting would be pointless at best, and potentially misleading. It is true that there is a sense in which the cost of items clearly subject to that paragraph – including those reported in the past – are opportunity costs. But they are also book costs, or portions of book costs which can be estimated by comparison with other scenarios such as a Medicare-integrated retiree health plan. The "cost" of refraining from, e.g., selling address lists is an opportunity cost only. We see no reason to believe that Congress meant non-book costs to be evaluated and reported under sec. 3651(b)(1)(C).[8]

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[7] Analysis, p. 2; fn. omitted.

[8] For an extensive discussion of the distinction, for postal regulatory purposes, of the difference between book and opportunity costs, see PRC Op. R83-1, ¶¶ 6027 et seq. In the course of that discussion, the Commission concluded that Congress used the term "cost" in the former (book cost) sense. (The issue was whether certain sums reasonably regarded as opportunity costs, in the economist's sense, should be attributed to the mail category in question; the Commission decided that they should not.)

Except for the suggestion just discussed, regarding “negative requirements,” GCA believes that the Postal Service’s Analysis is a clear and helpful basis for the Commission’s re-examination of the scope of sec. 3651(b)(1)(C) reporting.

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Respectfully submitted,

GREETING CARD ASSOCIATION

David F. Stover
2970 S. Columbus St., No. 1B
Arlington, VA 22206-1450
(703) 998-2568
(703) 998-2987 fax
E-mail: postamp@crosslink.net